LC

ROUTING AND RECORD SHEET

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SUBJECT: (Optional)

FROM:	EXTENSION	NO.
Legislative Counsel		DATE 4 August 1975

STAT

TO: (Officer designation, room number, and building)	DATE RECEIVED	DATE FORWARDED	OFFICER'S INITIALS	COMMENTS (Number each comment to show from whom to whom. Draw a line across column after each comment.)
1. DDA	-7 AUG 1975			
2. OGC	8/7/75	8.8.75		
3. DDCI Director	8/8	8/8		
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The House Ways and Means Committee is considering a possible revision of Federal Income tax treatment of income earned abroad, including current tax exempted allowances paid Federal employees. It is anticipated that the Committee may include a provision on this subject in a clean bill to be reported out in September. During the 93rd Congress you registered your concern over this possibility and the attached letter to OMB is intended to support a similar position by Secretary Kissinger in the face of pressure from Treasury officials to bring about some sort of Federal Income tax treatment of allowances paid Federal employees. This has been coordinated with the DDA and OGC.

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George L. Cary
LegislativeCounsel

ER -
Add DDS to distribution [illegible]

CENTRAL INTELLIGENCE AGENCY

Washington, D.C. 20505

DD/A 75-3679

OLC 75-1842

8 AUG 1975

Honorable James T. Lynn, Director
Office of Management and Budget
Washington, D.C. 20503

Dear Mr. Lynn:

I have a copy of Secretary Kissinger's letter to Secretary Simon of 12 July 1975 expressing concern with a provision in proposed legislation pending before the House Ways and Means Committee which would impose Federal Income taxes on certain allowances paid to Federal employees serving overseas. During the 93rd Congress, I wrote to Mr. Roy Ash on 10 December 1974 to express my concern about the adverse impact of a similar proposal on our overseas operations.

I fully endorse the views and recommendations in Secretary Kissinger's letter.

It is understood that the proposed amendment to Section 912 of the Internal Revenue Code, which currently exempts those allowances from Federal Income taxes, is being related to the proposed change in the treatment of income earned abroad by other Americans.

It is my understanding that Americans employed abroad by private enterprise are generally managerial or executive personnel, and that local nationals normally fill clerical and middle management positions. Federal agencies cannot follow this practice and assign many employees overseas in the middle and lower grades. The allowances paid these and other employees are important to assure that those who are directed (in the case of CIA) to serve abroad are not forced to absorb a financial burden in countries with a higher cost-of-living than that of the United States and to assure a standard of living consistent with requirements imposed upon them as representatives of the Federal Government abroad.

I am informed that two proposals are under consideration within the Executive Branch to deal with the overseas allowance question. One is to increase the allowances, and thus appropriations, to offset the taxes to be levied. The other, which deals solely with the housing allowance, would seek to establish a tax base figure equal to the amount an employee would reasonably be expected to pay for housing in the United States.

It is my view that in the long-run such adjustments would be burdensome and expensive to administer and inconsistent with the underlying concept of these allowances. They also could disrupt our efforts to reduce the number of personnel overseas and improve the efficiency of those who remain.

We are, of course, prepared to discuss both principles and procedures in much greater detail if that is necessary to demonstrate that the proposed changes would have a major adverse impact on the efficiency of our operations. I strongly urge the Administration to oppose a major change in the overseas allowance program at this time.

Sincerely,

/s/ Bill

W. E. Colby
Director

cc: Secretary of State
Secretary of the Treasury

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STAT OLC/LLM:baa (4 Aug 75) [redacted] 2

THE SECRETARY OF STATE

WASHINGTON

July 12, 1975

Dear Bill:

The Ways and Means Committee is considering that portion of the "Energy Tax and Individual Relief Act of 1974" dealing with foreign income. I have heard that the Administration is scheduled to testify before the Committee in early July.

One provision of the proposed legislation might be the taxation of allowances paid to government civilians serving overseas. This is of great concern to me since taxation of overseas allowances would have serious implications not only for the Department of State, but for all other government agencies with civilian employees serving abroad. If we are to retain the flexibility we need in the personnel administration of our overseas operation, we must insure that our personnel are not financially disadvantaged through the taxation of allowances which represent reimbursement to them for the unusual costs associated with their overseas assignments. Such allowances cannot and should not be considered incremental income to employees.

The Overseas Differential Act of 1960 (P.L. 86-707) which authorizes most of the overseas allowances in question, and the House and Senate Reports on that Act, clearly show Congressional recognition that service abroad entails expenses to employees above those which the employees would incur were they stationed in the United States. There has never been any intention to give overseas employees advantages over their colleagues who serve at home, but rather to treat them equally. I know that many misconceptions exist, both in and out of government, as to the true nature of overseas allowances and benefits. Where unbalanced treatment exists, I believe we are well on the way to correcting it and reestablishing a firm and clearly justified basis for the allowance program. I do not think these imbalances in application of law or regulation justify treating allowances as incremental income, however.

The Honorable
William E. Simon,
Secretary of the Treasury.

An Inter-Agency Committee on Allowances and Benefits is currently reviewing the existing structure of federal civilian overseas allowances and benefits to arrive at recommendations on a comprehensive allowance program which would, effectively and equitably, meet current requirements for overseas operations.

Since the treatment of allowances for tax purposes is an essential element of the entire allowance structure, all committee members were asked to comment on the proposed repeal of Section 912 of the Internal Revenue Code. There was general agreement that consideration of any change in the present tax treatment of allowances should await completion of the current inter-agency review, and that a flat repeal of Section 912 at this time would be grossly inequitable, prejudicial to the operations of foreign affairs agencies, and without significant benefits to overall U.S. Government operations.

I think a brief review of some of the more significant overseas allowances will show why it would be inappropriate to subject them to taxation. The essential feature of each of these allowances is that it is intended to defray necessary additional expenses incurred because of overseas service. With the exception of the hardship differential paid to employees at unhealthy, dangerous or otherwise less desirable posts, which is currently subject to taxation, none of the allowances are classified as "premium" allowances.

-- The cost-of-living allowance is simply an equalizer designed to offset the difference between the cost of living at an expensive foreign post of assignment and in Washington, D.C. It is not realistic to expect employees to pay additional taxes because prices are higher in some parts of the world. For example, the cost of living for U.S. Government civilian employees in Geneva is 54% higher than Washington; in Kuwait 30% higher; in Yaounde 46% higher; and in Caracas 14% higher.

-- An education allowance is authorized so that all parents employed by the Government overseas can provide their children with the level of education which is available to all children free in the United States. Clearly this is not incremental income and not properly taxable.

-- The quarters allowance is also an offset against extraordinary housing expenses which an employee encounters as a direct result of his assignment in a foreign country. The average yearly cost of rent and utilities for a typical government employee between 1974 and 1975 rose by $1,974 in Copenhagen, $314 in Ankara, $2,075 in Beirut, $1,953 in Geneva, $596 in Lima, and $114 in Bangkok. With shortages of adequate housing and spiralling rent and utility costs at most foreign locations, the quarters allowance continues to be necessary to assign the right person to the right post at the right time.

I recognize that there are differences of opinion as to whether this last allowance includes an element of additional compensation and if so, whether it is justifiable. In my opinion if an employee overseas is advantaged by this allowance we should examine the method of computing the allowance and attempt to correct it rather than act precipitously to tax the quarters allowance. In this connection I am confident that the Inter-Agency Committee composed of senior officers from twenty government agencies will thoroughly study the problems and recommend remedies designed to achieve the results that we all seek.

It has been suggested that it is necessary to tax the allowances of government civilians overseas because we want to treat them in the same manner as employees of private industry overseas. I do not believe that repeal of Section 912 will contribute toward equal treatment, when the conditions under which each group serves are vastly different in so many ways. No more should we suggest that taxation of military allowances and benefits would constitute equal treatment for civilian and military personnel. It must be recognized that we are dealing with three vastly different groups with different reasons for being overseas, needs and responsibilities. That fact alone argues for the need for separate treatment and different procedures to meet the specific needs of each group.

For all these reasons, I believe that the Administration's position before the Ways and Means Committee should be to recommend that allowances not be taxed, and that correction of deficiencies in the program be left to the Administration through the Inter-Agency Committee on Overseas Allowances and

Benefits for U.S. Employees which would keep the Congress informed of the progress of its work. I am sending a similar letter to Jim Lynn expressing my thoughts on this subject. I hope that both of you will agree with my very strong recommendations regarding the Administration's position on this issue.

Warm regards,

Henry A. Kissinger

CENTRAL INTELLIGENCE AGENCY

WASHINGTON, D.C. 20505

Executive Registry
74-6835

OLC 74-2512

10 DEC 1974

Honorable Roy L. Ash, Director
Office of Management and Budget
Washington, D. C. 20503

Dear Mr. Ash:

I wanted to advise you of my concern regarding section 311(b) of H. R. 17488 which would change the Federal income tax treatment accorded allowances for Federal employees overseas.

Agency employees are required to serve wherever their services are required, including assignments abroad involving arduous or hazardous circumstances. Overseas allowances permit such assignments to be undertaken without financial loss and in keeping with the living standards they are expected to maintain during their assignments.

The proposed change in H. R. 17488 in subjecting such allowances to Federal income tax vitiates these purposes. Moreover, in the face of enactment there would be a need to adjust such allowances upwards to offset the increased tax burden and it would appear that the indirect cost to the Government would offset any revenue gained.

My staff has received positive assurances concerning this matter from representatives of the Department of State, Department of the Treasury and OMB, but I did want you to know of my personal concern.

Sincerely,

W. E. Colby
Director

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cc: Secretary of State Secretary of the Treasury

USIA

7/7/75

The Honorable
James M. Frey
Assistant Director for
Legislative Reference
Office of Management and Budget
Washington, D. C. 20503

RE H. R. 17488

Dear Mr. Frey

Under present law, Section 912 of the Internal Revenue Code exempts from Federal income taxes the amounts received by our officers and employees as allowances when they are assigned to serve in foreign countries. These allowances relate to travel, education, housing and cost of living. For the private sector, Section 911 of the Code provides a tax exemption up to $25,000 of income earned abroad by foreign residents.

Last year, the Ways and Means Committee reported out H. R. 17488, a bill introduced by Mr. Mills. The bill would have repealed Sections 912 and 911 over a three-year period beginning in 1975. The bill would have replaced these exemptions with a new deduction for tuition payments for dependents of foreign residents limited, however, to $100 a month for each dependent; and with a new exemption for "municipal type services" provided by an employer to his employees.

Our basic position is that the repeal of the tax exemption of these allowances is premature and requires fuller consideration. For this purpose, an inter-agency committee has been created to address the issue of overseas allowances and benefits and the advisability of altering current tax treatment.

Should the bill in its present form be enacted into law, a severe adverse impact on the morale of our foreign service information officers and other employees should be anticipated. The full consequences of this

impact cannot be foreseen at this time. We should expect substantial pressures for financial relief by the employee organization which represents our foreign service personnel in collective bargaining. These pressures must be viewed with concern.

We are not unmindful of the reasons which led to the drafting of the bill the evenhanded tax treatment of all U.S. citizens residing overseas, whether employed by the U.S. Government or by a private employer. On the other hand, the bill would appear to ignore basic considerations present at the time allowances were brought into being by legislative action. They were designed to compensate for the unique living conditions imposed by foreign service. For example, it is exceptionally difficult for our officers to find housing overseas that compares both in price and quality with that available in the Washington, D. C. metropolitan area. This is the rationale of the housing allowance.

The education allowance consists of an amount not to exceed the cost of the elementary or secondary education which would be provided to dependents without charge by public schools in the United States. In certain cases the Government also provides an allowance for room, board and periodic transportation when adequate schools are not available at the post.

Officers and employees may be reimbursed home leave travel expenses for themselves and their dependents, together with subsistence during travel, to and from their overseas posts to their homes in the United States, on a periodic basis.

Finally, the Government also pays an allowance to the officers and employees to compensate for the portion of the cost of living at foreign posts that exceeds the cost of living in the District of Columbia.

With this background in mind, we offer the following provisional comments on the bill, subject to the final position that may be adopted as a result of the work of the inter-agency committee

-- With respect to the educational allowance, the cost of tuition, transportation, room and board should be excluded from gross income.

-- Travel expenses incurred in connection with home leave should be excluded from gross income.

-- While we do not disagree in principle with the taxability of housing allowances, we believe that a realistic formula should be established for the rental value of housing in Washington, D. C. in proportion to an officer's salary.

-- Cost of living allowances should not be subject to taxation.

If H. R. 17488 were to be enacted into law, we would recommend the adoption of provisions for greater delay than now proposed for the phase-out of the tax exempt status of the allowances.

The point should be emphatically made that subjecting these allowances to taxation in the future would further erode the income of those officers earning $36,000 a year whose salaries have been frozen at that level since 1969.

In view of the vital importance of these matters to the foreign affairs personnel, we strongly urge affirmative support by the Office of Management and Budget for the position advanced herein.

Sincerely,

STAT [redacted]

General Counsel and
Congressional Liaison

STAT bcc: I - [redacted]

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IPT - [redacted] (substance)
IGC - [redacted] in draft) 7/3

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